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Issues '98

June 1998

Fact Sheet #4: Transmission Issues

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We are inviting you to participate in Issues '98. This is a public process designed to give you an overview of and a context for major policy issues surrounding BPA's future. Your input will help BPA develop planning assumptions for our power and transmission rate cases. With the exception of cost cutting recommendations, Issues '98 will not be a decision-making process by BPA. Instead, your comments will help inform decisions made in other forums, both within the region and by Congress. This fact sheet focuses on just one set of the broad issues that will be considered. To learn more about how to participate in Issues '98 or for more information on other issues, call (800) 622-4519.

Introduction

BPA has provided access to its transmission system for a variety of wheeling customers for more than 40 years under Federal statutes different from those that govern most of the rest of the industry. Greater competition in power markets and the growth of national players is now creating demand for more uniform services and tariffs among transmission providers. The Federal Energy Regulatory Commission (FERC) is presiding over this change. One change may be legislation which provides for FERC jurisdiction over all transmission providers, including BPA. It may also result in a requirement to turn over transmission control to independent system operators (ISO's).

As change progresses in the other 46 states, the Northwest needs to be moving in the same general direction. This will have an effect on BPA, since it owns and operates about 80 percent of the Northwest's high voltage transmission capacity. BPA has already voluntarily complied with FERC open access directives. But, further changes will be needed to bring BPA transmission rates, terms, and conditions into line with national practices.

The Transition Board of the four Northwest governors is developing legislation that may change how BPA's transmission function is regulated. Even without legislation, the coming rate cases that will be conducted under the current functional separation (of generation from transmission) will have to deal with new functionalization, allocation, and interbusiness-line issues. Resolution of these issues will probably result in number of cost and revenue shifts.

Some of these issues will be resolved in the power subscription rate case that will get underway this fall, while others must wait until the subsequent transmission rate case, slated to begin in 2000. BPA will try to minimize uncertainty to customers resulting from this new bifurcation of ratemaking so that they can make informed decisions about power and transmission acquisition.

Background

National events to deregulate the electric utility industry are having an impact on transmission:

- The Energy Policy Act of 1992 was a catalyst for deregulating the electric generation industry and opening up transmission systems. It followed the deregulation of the airline, telecommunication, and natural gas industries.
- In 1997, FERC Orders 888 and 889 directed FERC-jurisdictional utilities to separate their wholesale power and transmission functions. BPA complied with this voluntarily.
- In 1997, several members of Congress introduced national electric energy deregulation bills that would further deregulate the industry. None of the bills have passed yet. Congress will likely enact legislation for electric industry restructuring in the next few years. Northwest legislators have begun drafting a "Northwest chapter," addressing our transmission issues including FERC regulation of BPA transmission and the recovery of any stranded power costs through transmission surcharges. The Transition Board is now trying to develop a regional consensus on these issues.
- In March 1998, the Administration's electricity competition plan said FERC's open access rules should apply to federal power marketing agencies (PMA's). One exception may be necessary to provide expanded opportunities to recover any PMA stranded costs – the billions invested in the federal power systems – because of statutory cost recovery obligations. BPA had already complied voluntarily with FERC's open access directives through our 1997 filing of transmission rates, terms, and conditions.
- California began operating an ISO on March 31, 1998. Some view this as the beginning of a national trend.
- In an April 1998 technical conference, FERC commissioners strongly urged the formation of ISO's and the participation of transmission owners in ISO's. ISO's may be a stepping stone to TransCo's – owner-operators of large consolidated transmission systems. DOE supports ISO's and encourages BPA (and other PMA's) to move toward ISO operations.
- Primarily large industrial consumers are demanding consistent and enforceable reliability standards. The historic cooperative approach to reliability under the North America Reliability Council (NERC) will likely become a mandatory regime under the new North America Electricity Reliability Organization (NAERO). An independent board would run NAERO, not a board from utilities. FERC would approve standards and enforcement. This change would have a direct effect on who controls decisions for all transmission owners.

Regional activities are following the trend of national events:

- The governors' Comprehensive Review of the Northwest Energy System in December 1996 called for the Northwest to form an ISO, and recommended that BPA should take part in the ISO.

It also recommended that transmission restructuring should promote the broadest possible bulk power market competition through (1) independence of transmission operations from the power merchant function, (2) non-discriminatory, open access transmission, (3) elimination of rate pancaking, and (4) providing for single contracts for service (“one-stop shopping”). The ISO should promote efficiency by coordinating planning, pooling resources, and reducing unscheduled flows and losses. It should ensure reliable service, minimize cost shifts and not increase risk to Treasury. The Comprehensive Review also recommended that Bonneville’s power marketing and transmission functions should be fully and legally separated and that the transmission function should be subject to “FERC equivalent” regulation. The Comprehensive Review created a Transition Board to help move the region toward implementing its recommendations. As implementation issues were explored, many soon found it might be difficult to fully separate BPA because of potential jeopardy to third-party debt obligations. The Transition Board decided instead to recommend functional separation of BPA and to concentrate on subjecting BPA’s transmission system to FERC’s open access requirements, with specific exceptions described below. The Transition Board plans to offer language to the Northwest congressional delegation for the “Northwest chapter” of deregulation legislation in July 1998.

- Eight senators in a June 19, 1997, letter to the Northwest’s governors called for removing barriers to BPA’s participation in a regional ISO.
- On March 5, 1998, work among utilities in eight western states on an ISO, called IndeGO, was put on hold. Before the announcement, eight of the original 21 utilities had already withdrawn because of concerns about cost shifts, cumbersome processes, and undemonstrated cost-effectiveness. None of the remaining participants had committed to join until after FERC and the states had completed review of the governance, tariff, contract and pricing structures.
- Shortly after IndeGO was put on hold, Washington Water Power Co. and six other utilities and transmission users proposed an independent grid scheduler (IGS) for the Northwest. A memorandum of understanding (MOU) was sent to approximately 10 utilities, large industrial customers, marketers and BPA for comment and signature. The group hopes to have the MOU signed in June 1998. As with IndeGO, signing means only to participate in the development of an IGS proposal. No party is obligated to execute any contracts developed as part of the IGS discussions. An IGS doesn’t eliminate rate pancaking – the multiple fees levied when power moves through multiple transmission systems to its final destination. FERC would not likely find that an IGS meets all the criteria of a full-fledged ISO.

Functional separation and Federal Power Act conformance

Congress enacted the Federal Power Act (FPA) in the 1930s to impose controls on investor-owned utilities and trusts in the sale and transmission of electricity. The act was one of many in an era of trust-busting and regulatory reform. It created a Federal Power Commission (FPC) to implement and carry out the regulation of the utilities. FERC subsumed the FPC in the 1970s.

FPA conformance would formally subject BPA’s transmission system to many of the same rules governing open access and ratemaking as now apply to investor-owned transmission systems. Though the BPA transmission system currently provides open access transmission, the proposal would formally subject BPA to FERC’s generic transmission rulemakings (like Orders 888 and 889). It would also impose many of FERC’s transmission pricing rules on BPA’s transmission rate proposals and require FERC approval of BPA’s transmission contracts.

Under the functional separation and open access operation that BPA accomplished pursuant to Orders 888 and 889, a number of significant changes in cost recovery must be addressed in the next BPA power and transmission ratemakings. Full conformance to the FPA could change BPA's transmission rate structure even further. The network transmission rates, for example, may need to include some costs currently assigned to power, such as the generation integration segment. The generation inputs to ancillary transmission services may move more costs between power and transmission in addition to those determined in the last rate case. Another possible change could be rolling in the costs of the southern intertie into the network rate, thereby eliminating pancaking on BPA's own transmission system. One more big issue is whether the General Transfer Agreements (GTA's), which BPA uses to move its power over intervening transmission systems to many of its wholesale power customers, will continue to be rolled into power rates or rolled into network transmission rates, or directly assigned to the GTA customer. Finally, the assignment of the costs of control area operating reserves to generation or to the loads served by the (transmission) operator will be an issue. While none of these changes would create any additional revenue requirement for BPA as a whole, individual customers may experience significant cost shifts, depending on their particular circumstances. The realistic range of possible outcomes could have the network transmission rate rising from its current \$12 per kilowatt-year, by anywhere from \$2 to \$12, depending on the potential changes made in the coming rate cases. Other transmission rates (such as intertie) and power rates could experience offsetting reductions. The Transition Board's "strawman proposal" for FPA conformance suggests that FERC should phase in any such cost shifts to avoid "rate shock."

Any transmission rate increase would reduce the future usefulness of a transmission surcharge mechanism that would serve as a backstop to power revenues (in order to assure BPA's full annual payments to the Treasury). But the need for such a surcharge would also be lessened by the offsetting relief of power rates from having to bear some of these costs.

The Northwest may have less control over BPA rates under FPA conformance. If BPA fully conformed to FPA, it would file rates directly with FERC. FERC would hold any evidentiary hearings in Washington, D.C., with an administrative law judge. However the Transition Board's "strawman proposal" recommends that evidentiary hearings be held in the Northwest. Judicial review would take place in the Washington, D.C., Federal Circuit Court, or the Ninth Circuit Court.

BPA currently tests and develops its rates in a regional hearing. The Administrator decides the rates on the basis of the record and is provided with some discretion by FERC. BPA files its rates with FERC. FERC approves the Administrator's decision or remands the decision to BPA. Appeals are reviewed in the Federal Ninth Circuit Court in San Francisco. It's cheaper and more expedient for many smaller Northwest customers and the public to participate in the current process than to take part in an evidentiary hearing in Washington, D.C.

Other changes could follow FPA conformance: BPA could be required to file its transmission contracts with FERC for acceptance and go through the same FPA review process as investor-owned utilities. Capital investments in the transmission system might have to be first approved by FERC in order for BPA to avoid having them later determined to be imprudent, and the cost of building and maintaining facilities could be borne more directly by those who currently benefit from them.

Next steps

While BPA has provided open access under non-discriminatory tariffs, further steps are needed if it is to bring its transmission rates, terms, and conditions in line with FERC's direction at the national level. Many of these issues will be debated in the power subscription rate case and the subsequent transmission rate case. In addition, the Transition Board's proposal on a draft "Northwest chapter" for

national legislation may lead to more fundamental changes.

The Northwest's customers, constituents, and tribal governments should provide input to legislative recommendations and to the rate cases as national trends shape the future of grid operations.

While making these changes, BPA's transmission business line will continue to replace aging equipment and maintain the system in a safe, reliable, environmentally responsible, and very cost-effective manner.

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